

AUDIT REPORT
RURAL WATER DISTRICT NUMBER 2
COUNTY OF OKMULGEE, OKLAHOMA
PRESTON, OKLAHOMA
NOVEMBER 30, 2013

RALPH OSBORN
CERTIFIED PUBLIC ACCOUNTANT
500 SOUTH CHESTNUT
P.O. BOX 1015
BRISTOW, OKLAHOMA 74010-1015

INDEPENDENT AUDITORS' REPORT

The Honorable Members of the Board of Directors
Rural Water District Number 2, County of Okmulgee, Oklahoma
Preston, Oklahoma

I have audited the accompanying financial statements of the business-type activities of Rural Water District Number 2, County of Okmulgee, Oklahoma as of and for the year ended November 30, 2013, and the related notes to the financial statements, which collectively comprise Rural Water District Number 2's basic financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statement that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, I express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for our audit opinions.

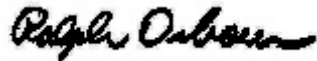
Opinion

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of Rural Water District Number 2 as of November 30, 2013, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Rural Water District Number 2 has not presented Management's Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statement.

In accordance with *Government Auditing Standards*, I have also issued my report dated September 8, 2014, on my consideration of Rural Water District Number 2's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of my audit.



Ralph Osborn
Certified Public Accountant
Bristow, Oklahoma
September 8, 2014

RURAL WATER DISTRICT NUMBER 2
COUNTY OF OKMULGEE, OKLAHOMA
PRESTON, OKLAHOMA
STATEMENT OF NET ASSETS
November 30, 2013

ASSETS

Current assets:

Cash and cash equivalents	\$ 84,772
Investments	135,847
Accounts receivable	62,423
Accrued interest receivable	316
Prepaid expense	12,989
Inventory	<u>53,688</u>
Total current assets	<u>350,035</u>

Non-current assets

Capital assets:

Land	46,510
Other capital assets, net of accumulated depreciation	<u>2,091,705</u>
Total non-current assets	<u>2,138,215</u>

Total assets	<u>2,488,250</u>
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LIABILITIES

Current liabilities:

Accounts payable	19,004
Accrued interest	876
Accrued vacation and sick leave	14,488
Notes payable, current	<u>24,938</u>
Total current liabilities	<u>59,306</u>

Non-current liabilities:

Notes payable, non-current	<u>759,138</u>
Total non-current liabilities	<u>759,138</u>

Total liabilities	<u>818,444</u>
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NET ASSETS

Nonspendable	1,415,943
Restricted for debt service	53,124
Unrestricted	<u>200,739</u>
Net assets of business-type activities	<u>\$ 1,669,806</u>

See accompanying notes to financial statements.

RURAL WATER DISTRICT NUMBER 2
COUNTY OF OKMULGEE, OKLAHOMA
PRESTON, OKLAHOMA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED November 30, 2013

OPERATING REVENUES

Charges for services:

Water sales	\$ 543,647
Water taps	8,025
Penalty	13,598
Other	<u>1,795</u>

Total operating revenues	<u>567,407</u>
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OPERATING EXPENSES

Water purchased	152,506
Salaries and wages	174,600
Payroll taxes	16,383
Insurance	43,118
Office	19,481
Administrative expense	17,615
Operating expense	29,985
Repairs and maintenance	57,028
Utilities	21,848
Miscellaneous expense	682
Depreciation	<u>82,149</u>

Total operating expenses	<u>615,395</u>
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Operating income (loss)	<u>(47,988)</u>
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NON-OPERATING REVENUE (EXPENSES)

Interest earnings	482
Interest on notes payable and fees	<u>(34,721)</u>

Total non-operating revenue (expenses)	<u>(34,239)</u>
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Change in net assets	(82,227)
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Total net assets, beginning	<u>1,752,033</u>
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Total net assets, ending	<u><u>\$ 1,669,806</u></u>
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See accompanying notes to financial statements.

RURAL WATER DISTRICT NUMBER 2
COUNTY OF OKMULGEE, OKLAHOMA
PRESTON, OKLAHOMA
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED November 30, 2013

Cash flows from operating activities	
Cash received from customers	\$ 565,865
Cash payments for employees and benefits	(182,687)
Cash payments to suppliers for goods and services	<u>(372,996)</u>
Net cash provided (used) by operating activities	<u>10,182</u>
Cash flows from capital and related financing activities	
Loan Proceeds	21,500
Acquisition of fixed assets	(57,419)
Interest paid on notes payable	(34,721)
Principal paid on notes payable	<u>(23,658)</u>
Net cash used for capital and related financing activities	<u>(94,298)</u>
Cash flows from investing activities	
Interest earnings	482
Transfer to investments	<u>(189)</u>
Net cash used by investing activities	<u>293</u>
Net increase in cash and cash equivalents	(83,823)
Cash and cash equivalents, beginning	<u>168,595</u>
Cash and cash equivalents, ending	<u><u>\$ 84,772</u></u>
Reconciliation of operating income (loss)	
to net cash provided by (used) by operating activities	
Operating income (loss)	\$ (47,988)
Adjustments to reconcile operating income to	
net cash used by operating activities:	
Depreciation	82,149
Changes in assets and liabilities:	
Decrease in accrued receivables	(1,662)
Increase in prepaid expenses	(932)
Increase in inventory	(21,853)
Increase in accounts payable	(7,948)
Increase in accrued interest	120
Increase in accrued vacation and sick leave	<u>8,296</u>
Net cash provided by operating activities	<u><u>\$ 10,182</u></u>

See accompanying notes to financial statements.

RURAL WATER DISTRICT NUMBER 2
COUNTY OF OKMULGEE, OKLAHOMA
PRESTON, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
November 30, 2013

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Rural Water District Number 2 (the "District") was created by the County of Okmulgee, Oklahoma Board of County Commissioners under the provisions of Title 82 Oklahoma statutes 1961, Sections 1301 to 1321 on August 30, 1965. The District is managed by a seven member Board of Directors elected by the members of the District. Terms of the Directors are staggered to expire in different years. Directors are elected at the annual meeting of the membership of the District. Membership in the District is acquired by paying a membership fee and receiving services from the District. The District is exempt from federal and state taxation.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The financial statements of the District are prepared in accordance with generally accepted accounting principles (GAAP). The District's reporting entity applies all relevant Governmental Accounting Standards Board (GASB) pronouncements and applicable Financial Accounting Standards (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless they conflict with GASB pronouncements. The District's reporting entity does not apply FASB pronouncements or APB opinions issued after November 30, 1989.

The financial statements report using the economic resources measurement focus and the accrual basis of accounting. Reimbursements are reported as reductions to expenses. Revenues are recorded when earned and expenses recorded when a liability is incurred, regardless of the timing of related cash flows.

Operating income reported in financial statements include revenues and expenses related to the primary, continuing operations of the District. Principal operating revenues are charges to customers for sales or services. Principal operating expenses are the cost of providing goods or services and include administrative expenses and depreciation of capital assets. Other revenues and expenses are classified as non-operating in the financial statements.

Investments

The District follows Governmental Accounting Standards Board (GASB) Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools," which requires marketable securities to be carried at fair value. The District considers highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. The investments reported in the financial statements consist of Certificates of Deposits.

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Inventories and Prepaids

Inventories consist of expendable supplies held for consumption stated on a first-in, first-out basis. They are reported at cost which is recorded as an expenditure at the time individual inventory items are used.

Prepaids record payments to vendors that benefit future reporting periods and are also reported on the consumption basis.

Capital Assets, Depreciation, and Amortization

The District's property, plant, and equipment, with useful lives of more than one year are stated at historical cost and comprehensively reported in the financial statements. Capital assets costing \$1,000 or more are capitalized and depreciated. Donated assets are stated at fair value on the date donated. The cost of normal maintenance and repairs that do not add to the assets value or materially extend useful lives are not capitalized. Capital assets are depreciated using the straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are moved from the respective accounts, and the resulting gain or loss is recorded in operations.

Estimated useful lives, in years, for depreciable assets are as follow:

Buildings	5-60
Improvements, other than buildings	2-50
Mobile equipment	3-40
Furniture, machinery, and equipment	3-30
Utility system	5-50

Reserves and Designations

Reserves represent those portions of net assets not available for expenditure or legally segregated for a specific future use. Designated net assets represent tentative plans for future use of financial resources.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

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November 30, 2013

Compensated Absences

Full-time, permanent employees are granted personal leave in varying amounts to specified maximums depending on tenure with the District. The estimated liabilities include required salary-related payments. Compensated absences are reported as accrued in the financial statements.

FUND TYPES AND MAJOR FUNDS

The District reports as a single fund special purpose entity.

NOTE B - DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS

Custodial Credit Risk

Custodial credit risk is the risk that in the event of failure of counterparty, the District will not be able to recover the value of its deposits or investments. Deposits are exposed to custodial credit risk if they are uninsured and uncollateralized. Investment securities are exposed to custodial credit risk if they are uninsured, are not registered in the name of the District, and are held by counterparty or the counterparty's trust department but not in the name of the District. The District's policy requires that all deposits and investments in excess of amounts covered by federal deposit insurance be fully collateralized by the entity holding the deposits or investments. As of November 30, 2013, all of the District's deposits and investments were either covered by federal deposit insurance or were fully collateralized.

Deposits

The District had deposits at financial institutions with a carrying amount of approximately \$220,619 at November 30, 2013. The bank balance of the deposits at November 30, 2013 was approximately \$230,808.

Credit Risk

Fixed-income securities are subject to credit risk. However, the District did not have fixed income securities at November 30, 2013.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Board of Directors monitor's the investment performance on an ongoing basis to limit the District's interest rate risk. As of November 30, 2013, the District's deposits consisted of demand deposits and certificates of deposit with a maturity of 12 months or less.

NOTE C - ACCOUNTS RECEIVABLE

The District records the total due on accounts owed for services unpaid at November 30. Any uncollectible amounts are written-off as they become uncollectible.

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NOTES TO FINANCIAL STATEMENTS
November 30, 2013

NOTE D - CAPITAL ASSETS

Changes in capital assets.

The following table provides a summary of changes in capital assets:

	CAPITAL ASSETS, DEPRECIATED			
		Improvements Other Than Buildings	Furniture, Machinery, And Equipment	Totals
	Buildings			
Balance, Nov. 30, 2012	\$ 72,630	\$ 3,054,687	\$ 177,503	\$ 3,304,820
Increases	-	-	11,909	11,909
Decreases	-	-	-	-
Balance, Nov. 30, 2013	<u>72,630</u>	<u>3,054,687</u>	<u>189,412</u>	<u>3,316,729</u>
Accumulated Depreciation				
Balance, Nov. 30, 2012	39,976	950,662	152,237	1,142,875
Increase	2,637	69,410	10,102	82,149
Decreases	-	-	-	-
Balance, Nov. 30, 2013	<u>42,613</u>	<u>1,020,072</u>	<u>162,339</u>	<u>1,225,024</u>
Other Capital Assets, Net	<u>\$ 30,017</u>	<u>\$ 2,034,615</u>	<u>\$ 27,073</u>	<u>\$ 2,091,705</u>
	Capital Assets Not Depreciated Land			
Business-type activities				
Balance, Nov. 30, 2012	\$ 1,000			
Increases	45,510			
Decreases	-			
Balance, Nov. 30, 2013	<u>46,510</u>			
Business-type Activities				
Capital Assets, Net	<u>\$ 46,510</u>			

RURAL WATER DISTRICT NUMBER 2
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PRESTON, OKLAHOMA
NOTES TO FINANCIAL STATEMENTS
November 30, 2013

NOTE E - NOTES PAYABLE

The District has incurred indebtedness for the expansion of system facilities and acquisition of equipment. The following is a summary of note payable transactions for the year ended November 30, 2013.

	Payable at Nov. 30, 2012	Retired/ Added	Balance at Nov. 30, 2013
Rural Development	\$ 600,329	\$ (8,493)	\$ 591,836
Rural Development	25,504	(5,375)	20,129
Rural Development	156,479	(5,048)	151,431
Citizens Security Bank	3,922	(3,922)	-
Citizens Security Bank	<u>-</u>	<u>20,680</u>	<u>20,680</u>
	<u>\$ 786,234</u>	<u>\$ (2,158)</u>	<u>\$ 784,076</u>

The notes payable are summarized as follows:

<u>Outstanding</u>	<u>Amount</u>
\$643,800 Note No. 91-08, issued by Rural Development with monthly payments of \$2,820, interest of 4.25%	\$ 591,836
\$110,700 Note No. 91-03, issued by Rural Development with monthly payments of \$544, interest of 5%	20,129
\$220,000 Note No. 91-06, issued by Rural Development with monthly payments of \$1,063, interest of 5%	151,431
\$21,500 Note, issued by Citizens Security Bank, with monthly payments of \$500, interest of 4.75%	<u>3,922</u>
Total	<u>\$ 784,076</u>

RURAL WATER DISTRICT NUMBER 2
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November 30, 2013

The Rural Development note agreements require a loan reserve equal to 12 months payments. The required loan reserve is \$53,124. The reserve at November 30, 2013 was in the amount of \$53,124.

Debt service requirements, including principal and interest, are as follows:

<u>Year Ended Nov. 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$ 24,938	\$ 34,186	\$ 59,124
2015	26,131	32,993	59,124
2016	27,382	31,742	59,124
2017	22,883	30,481	53,364
2018	16,938	31,834	48,772
2019-2023	121,955	135,766	232,980
2024-2028	127,451	111,025	232,980
2029-2033	112,652	93,836	221,287
2034-2038	139,272	56,548	169,200
2039-2043	139,272	29,928	169,200
2044-2045	67,260	3,240	70,500
	<u>\$ 784,076</u>	<u>\$ 591,579</u>	<u>\$ 1,375,655</u>

NOTE F - EMPLOYEE RETIREMENT PLAN

The District allows employees to participate in a SIMPLE IRA retirement plan. The employee may have up to 3% of salary withheld for the plan. The District matches up to 3%. Benefits from the plan will depend on the amount paid in plus earnings.

NOTE G - RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District carries commercial insurance, including workers compensation, for risk of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE I - WATER PURCHASE

The District purchases water for resale from City of Okmulgee, Oklahoma and from City of Beggs, Oklahoma. The District would not be able to replace the lost water if the City of Okmulgee, Oklahoma supply was interrupted.

Note J - SUBSEQUENT EVENTS

Management has evaluated subsequent events through September 8, 2014, the date on which the financial statements were available to be issued. The Authority does not believe there are any events requiring disclosure.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND
ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors
Rural Water District Number 2
Okmulgee County
Preston, Oklahoma

I have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of Rural Water District Number 2, County of Okmulgee, Oklahoma, as of and for the year ended November 30, 2013, and the related notes to the financial statements, which collectively comprise Rural Water District Number 2's basic financial statements and have issued my report thereon dated September 8, 2014 which did not include Management's Discussion and Analysis.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered Rural Water District Number 2's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing my opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Rural Water District Number 2's internal control. Accordingly, I do not express an opinion of the effectiveness of Rural Water District Number 2's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

My consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit I did not identify any deficiencies in internal control that I consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

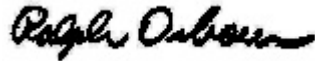
Compliance and Other Matters

As part of obtaining reasonable assurance about whether Rural Water District Number 2, County of Okmulgee, Oklahoma's financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of the Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Sincerely,



Ralph Osborn
Certified Public Accountant
Bristow, Oklahoma
September 8, 2014